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# **Social security and retirement reform**

*a progress report*

Andrew R Donaldson, National Treasury  
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# Interdepartmental task team: *work agenda*

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- **Social assistance grants – minimum benefits financed on budget**
- **Design of new social security contributory arrangements**
  - Basic pension
  - Extended unemployment benefits
  - Survivor and disability benefits
- **Social security governance and system framework**  
*Enrolment → Collection → Account administration → Fund management → Payment of benefits*
- **Coordination of administrative agencies and systems**
  - SARS, UIF, Compensation funds, Guardian's Fund, GEPP...
  - Possible “clearing house” partnership with private funds administration
- **Regulatory reform of retirement fund industry**
  - Preservation, portability
  - Mandatory savings – standard provisions
  - Proposals for a fund accreditation framework
  - Disclosure and control of costs
- **Links between employment, wages and social security**
  - Wage subsidy or cross-subsidy options
- **Tax treatment of retirement contributions and funds**
- **Complementary social insurance reforms**
  - Health insurance, RAF reform, occupational health and safety

## Social security, employment and poverty reduction

### Social security reform

- ✓ Extended social assistance net
- ✓ Broader social insurance: to reduce vulnerability to disability, death of breadwinners
- ✓ Support for employment & earnings of working poor; enhanced 'social wage'
- ✓ Support for saving and elimination of means test 'poverty trap'

### Anti-Poverty Strategy

- Income security
- Employment and second economy interventions
- Social cohesion and community development
- Housing and basic services
- Land redistribution and rural development
- Education and skills development
- .....
- .....

# Social security, employment and the budget

## Social security reform

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***Policy challenge: to improve alignment of social assistance and contributory income security***

## On budget programmes

- Social assistance grants
- Housing and basic household services
  - Education and skills development
  - Health services

## Employment-related benefits

- Retirement savings
- Death and disability insurance
- Occupational injury & disease compensation

## Social assistance – non-contributory “first pillar”

### Social grants expenditure as a percentage of GDP, 2003/04 to 2010/11

R million	2003/04	2007/08 Preliminary outcome	2008/09	2009/10	2010/11
			Medium term estimates		
Social grant expenditure	37 010	62 445	70 726	78 120	84 295
Administration	1 954	4 520	4 541	4 883	5 205
<i>Percentage of GDP</i>	<i>3.0%</i>	<i>3.3%</i>	<i>3.3%</i>	<i>3.3%</i>	<i>3.2%</i>

#### Beneficiary numbers (April 2008 est):

– Old age grant	2 225 354
– War veterans	1 931
– Disability	1 409 434
– Foster care	446 994
– Care dependency	110 153
– Child support	8 208 334

- **Reform proposals – 2008 Budget:**

- Raise means test thresholds
- Raise CSG qualifying age to 15 in 2009
- Equalise old age grant qualifying age for men and women by 2010

- **Under review:**

- Conditions to be applied to CSG caregivers
- Definitions of disability

# Social security design issues

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- **Basic contributory pension arrangement**
  - Savings 10-12 % of earnings
  - Defined benefit based on indexed lifetime earnings
  - Annuitisation at standard community rate
  - Extent of coverage, earnings floor for contributions
  - Mandatory participation in national fund, or opt-out of accredited schemes
- **Risk benefits (unemployment, disability and survivors):**
  - 5-6 % of earnings, up to present UIF threshold (R150 000 pa)
  - Extension of unemployment insurance – coverage of public sector
  - Unemployment insurance improvements – minimum benefit or employment guarantee; links with labour centre initiatives
  - Scope for coordination and alignment of disability and survivors arrangements (Compensation funds, disability and chronic illness assessment, Guardian's Fund, bargaining council and provident fund trustee responsibilities)
- **Collection by SARS, through PAYE system**
  - Requires individual contributor accounts to be maintained
  - Based on standard definition of remuneration
  - Extension to include informal sector and unregistered employers

## **UIF reform – *balancing labour market and income security needs***

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- **Consideration to be given to inclusion of public servants, migrant workers on fixed-term contract, learners and the self employed**
- **Adjustments needed to risk benefits provided by the state (UIF section 14 exclusions)**
- **Development of a framework for mitigating the risks of unemployment and activation measures aimed at re-integration into the labour market**
- **Extending the period of UIF benefits to be investigated, to provide for social assistance to those who remain unemployed beyond expiry of funded benefits**

## **Survivor benefits – *administrative challenge***

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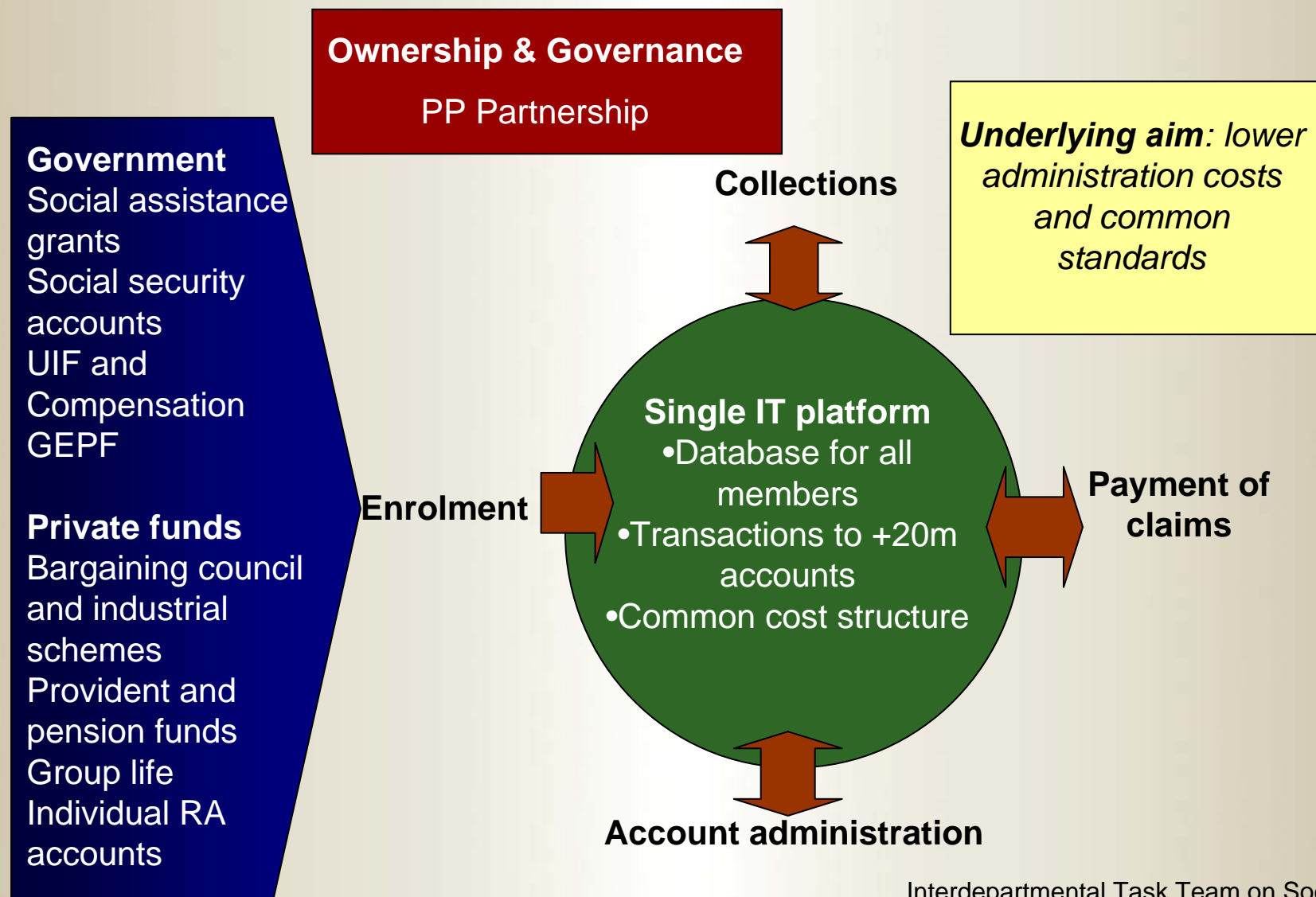
- **Present arrangements fragmented and inefficient**
  - Identification of beneficiaries and distribution of death benefits is onerous burden on trustees
  - Benefits vary widely
  - Delays and administrative failures common
- **Overlaps between death and disability insurance (“group life”), RAF and compensation funds arrangements**
- **Survivor benefits are not integrated with social assistance (child support and foster care grants)**
- **Guardian’s Fund administers orphans’ benefits on behalf of GEPF**
  - Systems outdated and inefficient
- **Large-scale administrative challenge**
  - Approximately 4 : 1 ratio of adult deaths to retirements

# Systems improvement and modernisation

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- **Scope for consolidation of existing government systems : social grants, the UIF, compensation funds and the Road Accident Fund**
- **Benefits: economies of scale in administration, simplicity and accessibility for beneficiaries, standardization of systems and integrated fraud control arrangements**
- **SASSA is largest payments infrastructure, currently makes use of regional payments contractors (using both banks and Post Office)**
  - **More efficient long term payments arrangements needed**
- **UIF administration has successfully enrolled household and agriculture employees and streamlined payments off an electronic platform**
- **Option of public-private partnership in administration clearing-house to be explored**

## A pensions and social security “clearing house”?



# Retirement fund industry reforms

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- **Transition to mandatory retirement provision involves several reforms:**
  - **Preservation of benefits and portability**
  - **Defined minimum benefits**
  - **Management of transaction costs and disclosure of fees**
  - **Development of common regulatory framework**
    - Pension and provident funds
    - GEPF and other exempt schemes
  - **Issues in annuity design**
  - **Standards for accredited (tax privileged) retirement funds**
  - **Provision for post-retirement medical contribution assurance**
- **Reducing costs means product standardisation, improved disclosure, capping of charges, managed competition**
- **Encouraging economies of scale – such as industry funds**
- **Regulatory and tax reforms are aimed at improving equity, efficiency and adequacy**

## Implications for tax system

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- **Consideration of combined payroll taxes (UIF, skills levy) in a consolidated social security contribution**
  - Public service included
  - Coverage issues to be considered: agriculture, self-employed, household employees
- **Offsetting wage subsidy and changes to the personal income tax structure**
- **Further reform of retirement fund & medical scheme tax deductibility to cap benefits & improve equity**
  - Tax encouragement of mandatory contributions to a basic savings element
  - Some tax encouragement of supplementary savings
  - No special tax treatment above a certain ceiling
  - Scrapping of RFT: improved retirement benefits
  - Simplification of formula applied to tax-free lump sum benefits
- **Administrative and systems capacity to manage individual contribution records**

# Wage subsidy proposal

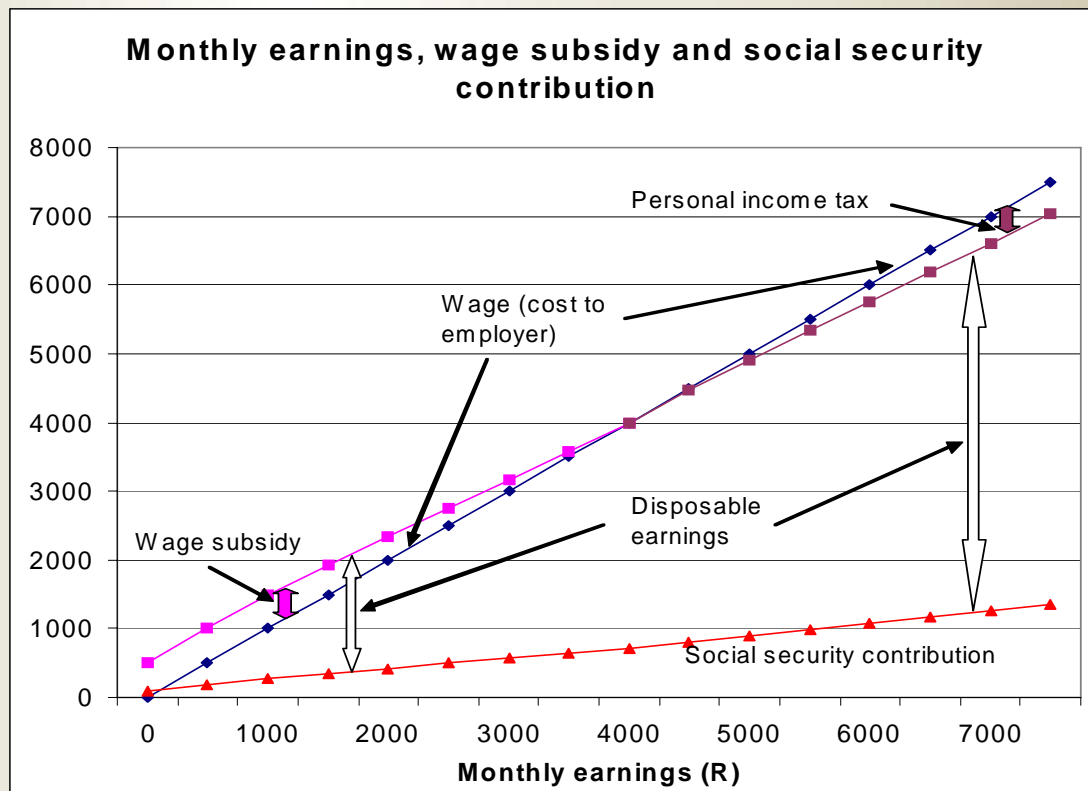
## Key features

- Aimed at supporting both job creation and wages of working poor
- Implementation as reimbursement to employers through PAYE tax credit
- Offset social security contribution for low-wage workers
- Design options: broad coverage, or targeted incentive (eg for young first-time workseekers)
- Cost: R20–30 billion

## Economic impact under review

### Alternatives to wage subsidy:

- Cross-subsidisation within social security system
- Contribution earnings threshold of R12 000 a year



Interdepartmental Task Team on Social Security and Retirement Reform

# Long run implications of social security reform

- SA needs to encourage job creation, social security has to avoid raising labour costs
  - Hence wage subsidy proposal
- Well-designed social security can support formalisation of employment & reduce dependence on welfare assistance
- Mandatory contributory savings & preservation of retirement benefits requires improved unemployment and risk (death, disability) benefits
- Earnings-related bridge between social assistance programmes & tax-privileged retirement, risk and medical scheme benefits contributes to overcoming “poverty trap”
- Illustrative modeling results: Impact of social grants (2), plus wage subsidy and social insurance (3), on poverty (R322 ppm in 2000 prices) by 2020:

	<i>Gini</i>	<i>Poverty head-count (million)</i>	<i>Income gap (R billion)</i>
1	0.63	15.3	60.2
2	0.61	12.6	31.9
3	0.57	9.7	21.0

*Cost: Social grants R63 billion; wage subsidy R31 billion; tax relief R22 billion*

*Source: Simkins, Social security projections*

# Assessment of progress to date

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- **Basic social security design**
  - Good progress towards a shared government view, further analysis needed
  - Will raise difficult issues for negotiation, for example relating to industry funds and preservation of retirement benefits
- **Institutional coordination of administrative arrangements**
  - Broad institutional governance option explored
  - Limited progress in interdepartmental consultation on administrative issues
- **Systems design and development**
  - Conceptual framework and “administration clearing house” model developed
- **Retirement regulation reform**
  - Legislative and regulatory reform is underway, including governance and market conduct
  - Sequencing of reforms & consultation with industry needs to be stepped up
- **Linkages with wider social security reform (SHI, RAF, labour policy)**
  - Options for post-retirement medical contribution protection explored
  - Wage subsidy discussion paper and evaluation model have been prepared

## Pension and social security law reform – *issues for discussion?*

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- **Overall system design issues:**
  - Tension between competition and regulation
  - Simplification and standardisation vs product variety and choice
  - Social security reform involves conversion of negotiated remuneration agreements and protection of existing rights
- **If “opt-out” arrangements are allowed:**
  - Social security cuts across administrative and contract law
  - Rules relating to transfers and risk-pooling needed
- **Sequencing of reforms can allow for lengthy transition**
  - “Dual” system would bring some complexity
- **Balance of risk between state, employers and contributors:**
  - Demographic
  - Economic and financial
  - Institutional and contractual
- **Social security is about long-term, shared interests**